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IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

IN THE MATTER
of
ASSOCIATED GAS AND ELECTRIC COMPANY,
Debtor.

IN THE MATTER
of
ASSOCIATED GAS AND ELECTRIC CORPORATION,
Debtor.

No. 241

IRVING ELIAS, MAX MENACHEN and MICHAEL MOISE, constituting the Protective Committee for the Holders of Convertible Obligations, Due 2002, etc.,
Petitioners,

against

STANLEY CLARKE, TRUSTEE OF ASSOCIATED GAS AND ELECTRIC COMPANY, Debtor, *et al.*,
Respondents.

No. 242

IRVING ELIAS, MAX MENACHEN and MICHAEL MOISE, constituting the Protective Committee for the Holders of Convertible Obligations, Due 2002, etc.,
Petitioners,

against

DENIS J. DRISCOLL AND WILLARD L. THORP, TRUSTEES OF ASSOCIATED GAS AND ELECTRIC CORPORATION, Debtor, *et al.*,
Respondents.

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

RESPONDENTS' BRIEF IN OPPOSITION.

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Glossary of Abbreviations.

Ageco	Associated Gas and Electric Company, Debtor.
Agecorp	Associated Gas and Electric Corporation, Debtor.
CDCs	Ageco Convertible Debenture Certificates and Convertible Debenture Obligations without fixed maturities.
CICs	Ageco 5½% Convertible Investment Certificates.
COs	Ageco Convertible Obligations, Series A and B, due 2002.
Non-Original Holders of COs	Holders of COs other than Original Holders.
Original Holders of COs	Holders of COs who obtained their securities in exchange for CDCs and still retain them.
Plan	Joint plan of reorganization of Ageco and Agecorp approved by the Securities and Exchange Commission and the courts below.

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ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

RESPONDENTS' BRIEF IN OPPOSITION

Opinions Below

The findings and opinion of the Securities and Exchange Commission, approving the joint plan of reorganization (Plan)[1] of Associated Gas and Electric Company (Ageco) and Associated Gas and Electric Corporation (Agecorp) under Section 11 (f) of the Public Utility Holding Company Act of 1935 [15 U. S. C. §79k(f)], have not yet been officially reported. They have been published in Holding Company Act Release No. 4985, and are set forth at R. 3347-3432.

The opinion of the United States District Court for the Southern District of New York (R. 152-277), approving the Plan under Section 174 of the Bankruptcy Act (11 U. S. C. §574), is reported at 61 F. Supp. 11.

The opinion of the United States Circuit Court of Appeals for the Second Circuit (R. 3570-3592), affirming the action of the District Court, is reported at 149 F. (2d) 996.

Jurisdiction

The judgments of the United States Circuit Court of Appeals for the Second Circuit were entered on April 19, 1945 (R. 3592-3594). The petition for writs of certiorari was filed on July 18, 1945. The jurisdiction of this Court is invoked by petitioners under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

Statute Involved

The statute involved is Section 174 of the Bankruptcy Act (11 U. S. C. §574), the pertinent portion of which provides as follows:

> "After the hearing, ***the judge shall enter an order approving the plan or plans which in his opin-

[1] A glossary of abbreviations used in this brief appears at page iii.

ion comply with the provisions of section 216 of this Act, and which are fair and equitable, and feasible, ***"

Question Presented

Is the Plan fair and equitable in its exclusion, as subordinate creditors of Associated Gas and Electric Company (Ageco), of the Non-Original Holders of Convertible Obligations (COs) of Ageco?

Statement

The petition for writs of certiorari seeks to carry into this Court a very simple issue, an issue which a long line of decisions of this Court clearly required to be resolved adversely to the petitioners. The attempt has been made, however, to surround this issue with an aura of complexity entirely foreign to the case. Petitioners have recited many facts which were relevant to the contentions of the other parties who appealed to the Circuit Court of Appeals from the orders approving the Plan (R. 321-328)[2], but which have no conceivable bearing upon the rights of Non-Original Holders of Convertible Obligations (COs). Those facts are not in point here, because the other appellants have not attempted to obtain review by this Court of the judgments below.

Petitioners have also made an elaborate presentation of facts which relate to the propriety of the order classifying them as subordinate creditors of Ageco (Elias R. 892-904).[3] Those facts serve only to obfuscate the issue here.

---

[2] The notice of appeal of petitioners was filed too late to be incorporated in the printed record on appeal.

[3] References to folios in the printed Transcript of Record heretofore filed in this Court in Nos. 590 and 591, October Term 1944, are designated by the notation "Elias R." By stipulations of the parties, that Transcript was made part of the printed record on appeal in the court below and on the present petition.

Their purpose is to enable petitioners to launch a flank attack on the order of classification which was affirmed by the Circuit Court of Appeals and which this Court refused to review. *Elias* v. *Clarke*, 143 F. (2d) 640 (C. C. A. 2), *cert. den.*, 323 U. S. 778. This attempt obliquely to obtain a reconsideration of the issues in an earlier case must necessarily fail.

The situation presented to this Court, once the irrelevancies are removed from the scene, is a familiar one in reorganization proceedings. The assets of the debtors, Ageco and its subsidiary, Associated Gas and Electric Corporation (Agecorp), are insufficient to provide in full for the claims of their unsubordinated creditors. The law demands, in this situation, that subordinate creditors (such as Non-Original Holders of COs) and stockholders be excluded from a fair and equitable plan of reorganization.

Petitioners do not question the inadequacy of the combined assets of Ageco and Agecorp to provide full satisfaction of the claims of creditors to whom Non-Original Holders of COs are subordinate. The value of the assets available to those creditors does not exceed $115,000,000 (R. 296, 3384), and the creditors of Agecorp alone—who clearly are senior to subordinate creditors of Ageco (R. 3409, 3589-3590)—have minimum claims of $189,421,095 (R. 297, 298). Nor can petitioners question their own status as subordinate creditors. The order affirmed in the *Elias* case, *supra*, classified Non-Original Holders of COs as subordinate to "the general creditors of Ageco, except holders of obligations convertible at Ageco's option into stock" (Elias R. 897-898).

Petitioners have not hesitated, however, to attempt to upset the effect of the classification order. Most of their

arguments are mere reiterations of the contentions which they unsuccessfully urged in the *Elias* case. What is more, only in one instance have they even purported to present any of the grounds for certiorari specified in Rule 38(5)(b) of this Court. We nevertheless believe it necessary or desirable to answer those arguments advanced by petitioners which have even a color of plausibility or propriety. For this purpose, some additional facts must be stated.

Most of the COs now outstanding were issued by Ageco in exchange for Convertible Debenture Certificates (CDCs), but many of them were issued originally for cash or in exchange for other types of securities (Elias R. 876, 883). If COs were issued directly in exchange for CDCs, and are still retained by the persons to whom they were so issued, they are said to be in the hands of Original Holders of COs. All other COs are in the hands of Non-Original Holders of COs. The security holders represented by the petitioners thus consist of:

> (1) Holders of COs issued originally for cash or in exchange for securities other than CDCs, whether the present holders are the original owners or transferees of the securities; and
>
> (2) Holders of COs who are transferees of persons who obtained their COs upon exchanges for CDCs (Elias R. 883). It is estimated that $8,850,616 principal amount of COs is held by such transferees (R. 292-293).

In the *Elias* case, *supra*, all these Non-Original Holders of COs were classified as subordinate creditors of Ageco. This decision was based primarily on the conclusion of the courts below that the subordination provisions of the COs (Elias R. 877-881) were enforceable in bankruptcy in accordance with their terms (Elias R. 854-856; p. 336).

The courts below also ruled, with respect to those pr esent holders of COs who are transferees of persons who obtained their COs in exchange for CDCs, that no cause of action for rescission of CDC exchanges passed with the transfer of the COs (Elias R. 847-850; pp. 330-33 1).

No adjudication was made in the *Elias* case o f the rescission claims of Original Holders of COs and hence the classification order there involved did not enco npass these claims (Elias R. 837-841; 897-898). It was s imply assumed, for the purpose of determining the rights of some of the Non-Original Holders of COs, that such resc ission claims could be successfully maintained (Elias R. 843). The validity of the rescission claims of Original Hold ers of COs has never been adjudicated by the District Court (R. 164-165). The claims were recognized to be reas onably disputable, and were disposed of, on that ground, by com- promise (R. 260-264). Original Holders of COs parti cipate in the Plan in accordance with the amount of their claims recognized by the compromise of their rescission claims (R. 124-125, 127).

POINT I.

The Plan is fair and equitable in its exclusion of Non-Original Holders of COs.

Under the absolute priorities rule, which is embodied in the requirement of a "fair and equitable" plan of reorganization prescribed by Section 174 of the Bankruptcy Act, subordinate creditors cannot participate in a plan if the claims of senior creditors are not provided for in full.

> *Group of Institutional Investors* v. *Chicago, M., St. P. & P. R. Co.*, 318 U. S. 523;
> *Marine Harbor Properties, Inc.* v. *Manufacturers Trust Co.*, 317 U. S. 78, 85;
> *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106;
> cf. *Otis & Co.* v. *Securities and Exchange Commission*, 323 U. S. 624, 634.

The assets of Ageco and Agecorp, as we have shown, are insufficient by far to provide in full for the claims of their unsubordinated creditors. The exclusion from the Plan of subordinate creditors, such as Non-Original Holders of COs, necessarily follows by reason of the absolute priorities rule.

None of the arguments advanced by petitioners has the slightest effect upon the validity of this proposition. Most of their contentions are nothing more than a re-hash of their position in *Elias* v. *Clarke*, 143 F. (2d) 640 (C. C. A. 2), *cert. den.*, 323 U. S. 778, although they are carefully disguised. We shall dispose of their contentions seriatim.

A. The participation of CICs and CDCs.

Non-Original Holders of COs were classified in the *Elias* case, *supra,* as subordinate to all general creditors of Ageco "except holders of obligations convertible at Ageco's option into stock" (Elias R. 897-898). Petitioners argue that, by reason of the quoted exception, they are not subordinate to holders of obligations convertible at Ageco's option into stock. From this premise, with which we do not disagree, they draw the conclusion that all holders of COs are entitled to the same treatment under the Plan as is accorded holders of any securities which are so convertible. They point to the participation under the Plan (R. 125, 126) of the 5½% Convertible Investment Certificates (CICs) and the CDCs, and assert that, since these securities are convertible into stock at Ageco's option (Elias R. 574-577, 692-698), the COs should participate on a like basis with the CICs and CDCs.

We shall assume, *arguendo*, that the CICs and CDCs are among the securities encompassed by the exception in the order classifying Non-Original Holders of COs. But the CICs and CDCs, unlike the COs, contain no subordination provisions (R. 3588; Elias R. 560-585, 703), and rank on a parity with the very creditors to whom the COs are subordinate. The fallacy of petitioners' argument lies in their refusal to accept the simple principle of marshalling adopted in *Bird & Sons Sales Corporation* v. *Tobin,* 78 F. (2d) 371 (C. C. A. 8), and approved by the court below in the *Elias* case (Elias R., p. 336). By dint of such marshalling, any share of the assets which might ordinarily be distributable to the COs would have to be turned over to the general creditors to whom they have subordinated themselves (Elias R. 857-860). The marshalling would not alter the amount of the participation of the CICs and CDCs; it would simply increase the participation of general creditors other

than holders of CICs and CDCs, with the resulting exclusion of the COs.

In other words, the participation of the CICs and CDCs under the Plan cannot possibly redound to the benefit of the excluded COs. As long as the general creditors, other than the CICs and CDCs, are not provided for in full—and the value of the assets of the estates is such that they are not and cannot be provided for in full—, Non-Original Holders of COs, who are subordinate to those general creditors, cannot share in the assets (R. 3588-3589).

B. Lack of consideration for the subordination clause.

The argument that the subordination clause in the COs is void for want of consideration is a direct attack upon the validity of the classification order affirmed in the *Elias* case, *supra*. For that reason, it was summarily disposed of—not "ignored", as the petition put it (p. 19)—by the court below (R. 3588), and is not properly presented to this Court. We consequently find no cause to repeat here the complete answer to this argument which we submitted in the *Elias* case.

C. Participation of Original Holders of COs received upon exchange for certain CDCs, 1931 Series.

Petitioners contend that all holders of certain COs which were issued originally in exchange for a portion of the CDCs, 1931 Series, are entitled to participate in the Plan, whether or not those COs are in the hands of the persons who made the exchanges (Original Holders). This argument affects few of the Non-Original Holders of COs, and is really disposed of by the decision in the *Elias* case, *supra*. It nevertheless is probably desirable that we comment briefly on it.

There are two flagrant errors in the argument. In the first place, it assumes that the claims of Original Holders of those COs have been finally adjudicated, and that they participate under the Plan because their rescission claims were allowed. This is not so. It is true that the Special Master ruled in the *Elias* case that this small group of Original Holders of COs should be accorded the status of unsubordinated general creditors of Ageco (Elias R. 788-789). But his conclusion, contrary to the assertion made in the petition to this Court (p. 19), has been very much questioned. Exceptions to the Special Master's report were filed by a number of the parties, including the Agecorp Trustees (R. 3297-3304), and his ruling has never been confirmed by the District Court (R. 164-165).

The participation in the Plan of this small group of Original Holders of COs, like that of all other Original Holders of COs, is based upon the disputable character of the issues presented by their rescission claims and the litigation strength of those claims (R. 305-306). If these particular Original Holders of COs were compelled to rely upon the terms of their securities, of course, they would clearly have to be excluded; under the decision in the *Elias* case, the subordination provisions in their COs would be enforced. This small group of Original Holders of COs participates only by virtue of the settlement of their disputed claims to rescind the transactions whereby they exchanged their CDCs, 1931 Series for COs (R. 3407-3411).

The second error in the argument of petitioners lies in their failure to recognize that, even if any Original Holders of COs had rescission claims which would entitle them to be treated as general creditors, it would not improve the position of transferee holders of COs. This follows from the ruling of the court below in the *Elias* case, to which it

referred in its opinion on the Plan (R. 3588), that rescission claims did not pass with the COs, so that transferee holders of COs cannot assert such claims.

D. "Discrimination" between Non-Original Holders of COs and other security holders of the "same rank".

Petitioners' last argument is their only contention which even purports to present any of the grounds for certiorari specified in Rule 38(5)(b) of this Court. It is their position that the decision below sanctions discriminatory treatment in a plan of reorganization between creditors of the same rank and class, a result which plainly would be in conflict with many decisions of this Court.

The flaw in the argument, of course, is its assumption that Non-Original Holders of COs are creditors of the same rank and class as holders of CICs and CDCs and Original Holders of COs. The fundamental difference between the position of holders of CICs and CDCs and that of Non-Original Holders of COs—the former have no subordination provisions in their securities—has already been discussed (*supra*, pp. 8-9). The difference between the position of Original Holders of COs and that of Non-Original Holders of COs is equally substantial.

If Original Holders of COs had no rights other than those arising from the terms of their securities, they could not possibly participate under the Plan. As holders of COs, they would be subordinate creditors of Ageco and, like the other holders of COs, would be excluded from the Plan. But Original Holders of COs have asserted claims against Ageco based upon facts wholly extrinsic to the terms of their securities. Those rescission claims were disputed and then were recognized in the Plan, by way of compromise, at a small percentage of their face amount (R. 260-264). Original Holders of COs thus participate solely on the

basis of their right to assert rescission claims of a type which Non-Original Holders of COs, under the decision in the *Elias* case, *supra*, are not in a position to assert.

It is obvious, therefore, that petitioners' real complaint is not with the decision below in this case, but with the decision in the *Elias* case. What troubles them is the earlier ruling of the Circuit Court of Appeals that rescission claims of Original Holders of COs did not pass, without an express assignment of the claim, to transferees of the securities. The fact remains, though, that Original Holders do have some rights—their disputable rescission claims—which Non-Original Holders of COs, under the decision in the *Elias* case, do not possess. And therein lies the reason, entirely consonant with the bankruptcy theme of equality of distribution, for the more favorable treatment under the Plan of Original Holders of COs. Equality of distribution is not required, and in fact would violate the absolute priorities rule, where there is a disparity in claims.

The attack upon the court below for its application of New York law in the *Elias* case is belated and without merit.[4] The decisions of this Court (e.g., *Prudence Realization Corp. v. Geist*, 316 U. S. 89) as to the non-applicability of State law to the distribution of the assets of a bankrupt, are not concerned with the problem of determination of claims against the estate. It is true that a court of bankruptcy need pay no heed to State laws governing the distribution of the assets of an insolvent. But, in determining the validity or extent of claims against the estate, as distinguished from their rank, bankruptcy courts do follow local law.

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[4] This facet of petitioners' argument is relevant, of course, only to those Non-Original Holders of COs who have COs originally issued to their transferors in exchange for CDCs. See *supra*, p. 5.

In re Ten Eyck Co., Inc., 126 F. (2d) 806 (C. C. A. 2);

In re Weidenfeld, 277 Fed. 59 (C. C. A. 2);

3 COLLIER ON BANKRUPTCY (14th ed. 1941) 1762-1763;

2 REMINGTON ON BANKRUPTCY (4th ed. 1940) §955;

FINLETTER, THE LAW OF BANKRUPTCY REORGANIZATION (1939) 259.

The court below, in the *Elias* case, abided completely by these fundamental rules. The determination of the enforceability of the subordination provisions of the COs was made with reference to the Bankruptcy Act and, particularly, its theme of equality of distribution. The court reached the conclusion that subordination agreements of the type contained in the COs were enforceable under the Act (Elias R., p. 336). In determining whether certain Non-Original Holders of COs had any provable claims for rescission, on the other hand, the court properly looked to New York decisions governing the rights of transferees of securities (Elias R., p. 330).

Even if "federal law", rather than local law, governed this question, moreover, there is not a single decision, nor any consideration of public policy, which would have commanded a different result. The authorities cited in the petition (pages 24-25) all dealt with situations where there were specific assignments of claims. In our case, of course, the rescission claims were not assigned to Non-Original Holders of COs when they acquired their securities (Elias R. 843-844; 883-884; pp. 330-331).

Conclusion.

The decision of the court below is correct, and no sufficient reason has been advanced for its review by this Court. The petition for writs of certiorari should therefore be denied.

Dated, New York, N. Y., August 27, 1945.

Respectfully submitted,

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